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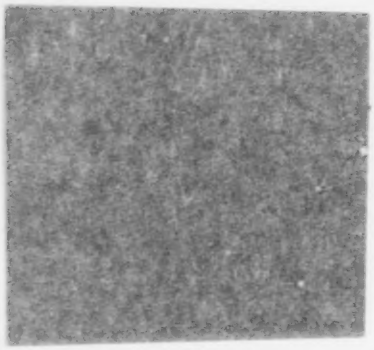

FINANCIAL SITUATION OF UNIDO

Submitted by the Director-General

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Introduction

1. At the beginning of the fourth quarter of 1997, the Organization found itself on the verge of a potentially disastrous financial crisis caused by the delay in the payment of assessed contributions by some Member States. The recent payment by a major contributor has temporarily averted the crisis, but the possibility of further financial crisis cannot be ruled out. Action taken by the Secretariat to delay the implementation of the budget to reduce cash outgoings will have a negative impact on programmes.

2. The present document provides information on the cash-flow crisis, borrowing, regular and operational budget implementation and the separation indemnity reserve. However, emphasis is placed on the cash-flow crisis resulting from delayed contributions from Member States, borrowing, the status of the Working Capital Fund and the situation resulting therefrom.

I. CURRENT SITUATION—REGULAR BUDGET

A. Cash-flow crisis

3. The partial, delayed or non-payment of assessed contributions by some Member States has placed the Organization in a very serious and unprecedented cash crisis. For the nine-month period ended 30 September 1997, assessed contributions received for the current and prior years amounted to only $66.9 million. During the same period in 1996, contributions received were $80.6 million. Thus, the contributing factors for the cash-flow crisis at that time comprised a shortfall in receipts of $13.7 million in 1997, and non-payment or partial payments by 11 major Member States, which owed UNIDO $43.3 million. This amount did not include the arrears of $60.3 million by the United States of America.

4. As of 30 September 1997, the available UNIDO cash balance was just $8.5 million, which was hardly sufficient to meet the Organization's requirements for one month. The fully depleted Working Capital Fund made the situation even more alarming. There was thus a high risk of UNIDO becoming insolvent, being unable to meet staff salaries and its obligations to suppliers, and putting in jeopardy its successful reforms. The trend of cash flows showed that UNIDO risked defaulting on its November obligations, including staff salaries. The situation could have resulted in serious difficulties for suppliers and staff, who would not have been able to meet their own financial obligations. Such a situation would have been tantamount to making suppliers and staff assume responsibility for the situation arising from the non-fulfilment of obligations by some Member States. UNIDO's financial credibility and good name would have been damaged and legal steps against the Organization could not have been ruled out.

5. To allay the crisis, the Director-General initiated a number of steps. He met with some Permanent Representatives of Member States and the Chairman of the Programme and Budget Committee, and dispatched special letters to all Member States urging them to pay their dues. He also sought guidance from those 57 Members, which had fully paid, in the collection of arrears by other Member States. The Director-General also deferred the implementation of various budgeted activities. In addition, the Secretariat requested the Government of Austria to accelerate the processing of the value-added tax claims of UNIDO to enable the Secretariat to meet some of its obligations, in particular to small suppliers.

6. Since there was no confirmed information on the timing of payment of assessed contributions by Member States, and a cash shortfall of $4.7 million was projected for November (PBC.13/CRP.6, annex III), the Director-General planned to temporarily borrow all available cash from the operational budget income account, the separation indemnity reserve and the 1992-1993 surplus account, amounting to around $7.5 million. In addition, the Director-General explored the possibility with the Government of Austria that it might advance an amount of 200 million Austrian schillings (about two months' cash requirement of the Organization) once the General Conference had approved borrowing. The Secretariat explored the prospects of borrowing from banks to overcome the immediate cash-flow problem. It should be noted that several United Nations specialized agencies, such as UNESCO, ITU and ILO, have resorted to this type of financing when they faced such a situation after having been so authorized by their policy-making organs on the basis of their financial regulations. UNIDO has never had to resort to this type of financing but, when, in 1986 it became a specialized agency, UNIDO received a loan of $16 million from the United Nations. UNIDO has already repaid $8 million against that loan.

7. On 29 October 1997, the Organization received two payments amounting to $1,510,267 and Austrian schillings 142,871,634 from a major Member State. These payments resulted in the situation where the immediate financial crisis was averted temporarily, but did not solve the problem of a possible future cash-flow crisis. Should further contributions not be received before the end of December, the Organization risks defaulting on some financial commitments in December, as well as on commitments for January 1998.

8. The year-end cash balance projection of $3 million (PBC.13/CRP.6, annex III) still does not cover the outstanding obligations, nor replenish the Working Capital Fund, which requires $6.75 million to be replenished. Cash availability continues to be a critical issue.

B. Borrowing

9. As reliable information is not received from many Member States as to when their assessed contributions will be paid, cash planning is made on the basis of past payment patterns in terms of amounts and timing. UNIDO is heavily dependent on the cash payments of its 12 largest contributors, which pay around 72 per cent of the total assessed contributions. These Member States generally fully pay their contributions on a regular basis. However, when payments from these Member States are not received as planned, UNIDO is confronted with an immediate financial crisis, as was the situation in October 1997. As of 30 September 1997, the contributions received from these 12 Member States, in United States dollar equivalent, amounted to $43 million. In comparison, the contributions received during the same period in 1996 were $52.3 million (see table 1 below).

10. In view of the uncertain pattern of payment by Member States, and in the absence of authority to borrow funds from Member States and/or financial institutions, the Organization could, at short notice, become unable to meet its financial commitments. The Organization, therefore, requires a mechanism to effectively address such short-term financial shortfalls. In view of the need for immediate steps to be taken to address sudden cash shortfalls, it would not be practical or cost-effective to convene extraordinary sessions of the policy-making organs for this purpose. For this reason, the Director-General seeks the authority of the General Conference for limited borrowing powers to overcome such cash crisis.

11. The Director-General recognizes that borrowing is no substitute for the fulfilment by Member States of their constitutional requirement for prompt and full payment of assessed contributions. Nevertheless, in the absence of an authority to borrow, and with a fully depleted Working Capital Fund, the Organization cannot function smoothly and fully execute its programmes in the current environment of cash-flow uncertainty. In the absence of an authority to borrow, there is potential risk that UNIDO could default on its financial commitments, including staff salaries, leading to disruption and additional costs, and damage to the Organization's reputation.

12. Since the Financial Regulations are silent on the borrowing authority, the Director-General requires the authority from the General Conference to negotiate and contract short-term loans from Member States, and/or if necessary, from financial institutions, when the cash situation of the Organization so requires, to enable the Organization to meet its financial commitments. As other United Nations specialized agencies have experienced financial crises similar to those of UNIDO, their Executive Heads have already been given such an authority (see PBC.13/CRP.7). The funds would be borrowed under the most favourable terms and conditions, and would not exceed more than a three-month cash requirement of the Organization, or 25 per cent of the approved annual budget at any time. UNIDO would not expect to provide security or collateral for the funds borrowed. Interest payments, if any, would be charged against miscellaneous income.

C. Status of assessed contributions and the Working Capital Fund

(a) Status of assessed contributions

13. The status of assessed contributions to the regular budget as of 30 September 1997 is shown in document PBC.13/CRP.6, annex I. Total outstanding contributions amounted to $117,347,350 (at an exchange rate of US$ 1 = AS 12.70), which included unpaid 1997 assessed contributions of $27,067,830 and arrears for the period 1986 to 1996 of $90,279,520, including the United States of America's arrears of $60.25 million. As opposed to this, using a comparable exchange rate, the total amount outstanding as of 30 September 1996 was $103.3 million.

14. As of 30 September 1997, the collection rate for the 1997 assessed contributions was 66 per cent, whereas at the end of the same period in 1996, the rate was 76 per cent. A total of 57 Member States, including six least developed countries, had made full payment of their 1997 assessed contributions. In addition, 34 Member States had made partial payments of their current and/or prior years' assessments as compared to 40 States in 1996.

15. Also, as of 30 September 1997, a total of 59 Member States had lost their voting rights in the General Conference due to non-payment of their dues in accordance with Article 5.2 of the Constitution and financial regulation 5.5(b). In addition, three Member States in the Programme and Budget Committee and five in the Industrial Development Board had lost their voting rights in those policy-making organs.

Table 1
Payment of current year assessed contributions
(As at 30 September 1997)

	1997	1996
Number of Member States	169	169
Members paid in full	57	52
Members made partial payment (current and or prior years)	34	40
Members made no payment	62	61
Members made no payment since joining UNIDO	16	16
Members lost voting rights (GC)	59	57
Members lost voting rights (IDB)	5	7
Members lost voting rights (PBC)	3	3
Total contributions received (current and prior years)	$66.9 million	$80.6 million
Collection rate (current year's assessments)	66%	76%
Total outstanding contributions	$117.3 million	$103.3 million (at AS 12.70)
Total amount due from 12 major States	$55.9 million	$55.6 million
Amount received from 12 major States	$43 million	$52.3 million

(b) Status of the Working Capital Fund

16. The status of advances to the Working Capital Fund is shown in document PBC.13/CRP.6, annex II. Unpaid advances as of 30 September 1997 amounted to $51,281. The Fund presently has no cash balance and it is not expected to be replenished to its authorized level of $6,750,000. The replenishment of the Working Capital Fund is critical for UNIDO's operation, as these funds are vital to finance budgetary appropriations pending the receipt of contributions.

D. Regular budget performance report

17. The financial implementation of the regular budget for the period January 1996 to September 1997 was subject to delays because of the need to ensure that cash disbursements be kept within available cash resources.

18. The financial indicators for the regular budget and contingency plans are presented in table 2 and figure 1 below. A more detailed presentation of the financial implementation by major programme and major object of expenditure is shown in annex IV to document PBC.13/CRP.6.

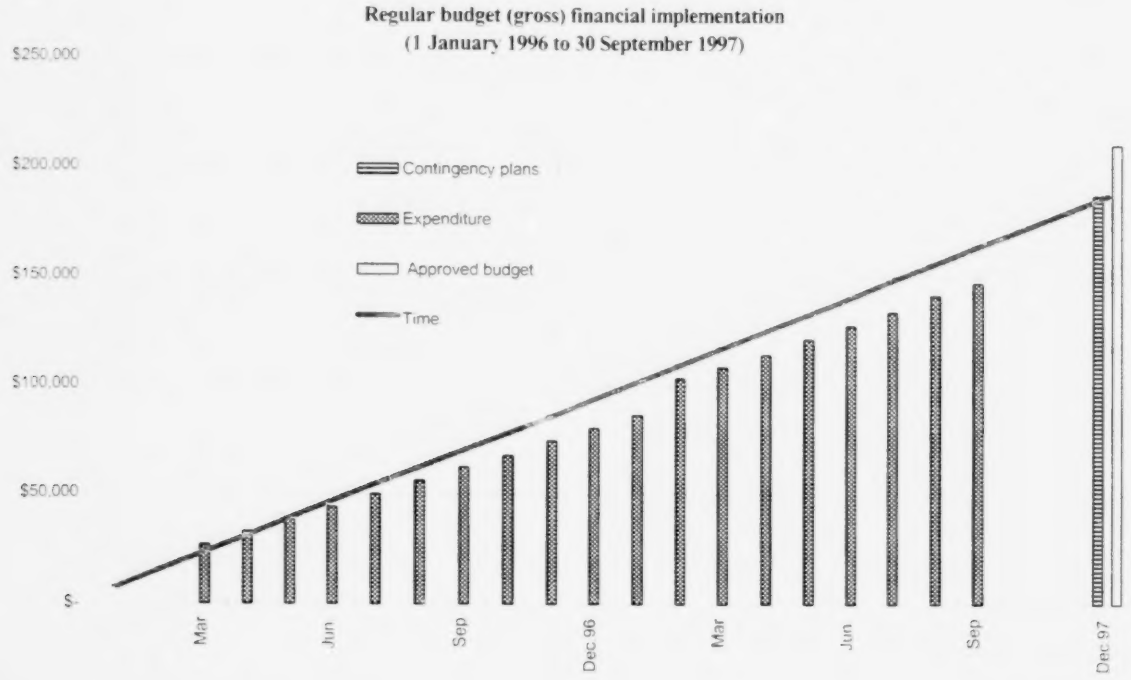
19. Full implementation of the programme and budget is dependent on the availability of cash resources throughout the biennium to permit a phased and smooth implementation. As a result of the cash crisis, full financial implementation of the budget is not expected. Reduced budget expenditures are also anticipated due to an increasing vacancy factor for Professional-level posts (13.4 per cent as at 30 September 1997). However, every effort is being made to ensure that the budgetary allocations for the Regular Programme of Technical Cooperation (RPTC) and Industrial Development Decade for Africa (IDDA) supplementary activities are fully utilized by the end of the biennium.

20. The rate of implementation is expected to increase during the final quarter of the biennium. Programme implementation will be accelerated, particularly in respect of RPTC and IDDA supplementary activities. Deferred payments and other budgetary expenditures, such as conference servicing costs related to policy-making organs sessions are expected to be incurred before the end of the year.

Table 2
Regular budget financial implementation
1 January to 30 September 1997
(In thousands of dollars at US$ 1 = AS 12.90)

Gross	Approved budget	Contingency plan
1996-1997	210,246.6	187,103.2
Expenditure to date	146,806.9	146,806.9
Unspent budget	63,439.7	40,296.3

Figure 1



II. OPERATIONAL BUDGET

21. The improvements to the financial situation of the operational budget experienced in the first seven months of 1997 and reported in document IDB.18/14-PBC.13/13 have continued.

22. As a result of improving technical cooperation delivery levels and a constant monthly outflow of expenditures, the operational budget is expected to achieve a surplus of approximately $140,000 for the year. This surplus will be used to strengthen the operating reserve, which had a balance of $3,374,900 at 31 December 1996.

23. The operational budget status report showing actual and projected income and expenditures for 1997, together with the estimated reserve balance at year-end, is summarized in table 3 below.

III. SEPARATION INDEMNITY RESERVE

24. The separation indemnity reserve was established in December 1995 at a level of $17 million for the purpose of funding and accounting for the costs of the staff reduction exercise. The utilization of the reserve and the unspent balances as at 30 September 1997 are shown in table 4.

Table 3
Operational budget status report, 1997
(In thousands of US dollars)

Opening balance of reserve - 1 January 1997			3,374.9
Income			
Actual - January to September 1997	9,438.1		
Projected - October to December 1997	2,812.8		
		12,250.9	
Expenditure			
Actual - January to September 1997	9,258.9		
Projected - October to December 1997	2,855.1		
		12,114.0	
Estimated surplus/(deficit)			136.9
Estimated closing balance of reserve - 31 December 1997			3,511.8

Table 4
Separation indemnity reserve
(In thousands of US dollars)

Approved level		
(a) Obligation against 1994-1995 budget appropriation		7,453.3
(b) Unutilized balances of appropriation for 1992-1993		9,546.7
		17,000.0
Utilization (30 September 1997)		
(a) Termination costs:		
Disbursements	(14,104.6)	
Obligations	(368.9)	
		(14,473.5)
(b) 1994-1995 obligations not utilized[a]		(567.7)
Balance of the reserve at 30 September 1997		1,958.8

[a] Included in the budgetary surplus for 1994-1995.

25. The balance of the reserve at 30 September 1997 is approximately $2 million. In view of the anticipated budgetary reductions for the 1998-1999 biennium, the balance of the reserve should be utilized to fund a limited number of the staff separations necessary to reduce the current staffing establishment to the anticipated 1998-1999 budgetary level. The issues related to staff separation and the separation indemnity reserve are discussed in detail in document IDB.18/15/5/Rev.1-PBC.13/14/5/Rev.1.

IV. ACTION REQUIRED OF THE COMMITTEE

26. The Director-General urges the Committee to take the required decision to address the cash-flow crisis arising from partial, delayed or non-payment of assessed contributions by Member States. The Committee may wish to recommend to the Industrial Development Board the adoption of the following draft decision:

"The Industrial Development Board:

"(a) Takes note of the report of the Director-General on the financial situation of UNIDO (GC.7/20-IDB.18/20-PBC.13/15) containing information concerning the 1997 cash-flow crisis, borrowing, status of assessed contributions, advances to the Working Capital Fund, regular budget performance, operational budget status and the separation indemnity reserve;

"(b) Notes that, despite considerable efforts made by the Secretariat, the collection rate of assessed contributions is continuing to deteriorate; the total amount of accumulated arrears as of 30 September 1997 stood at the equivalent of $117.3 million, as compared to $103.3 million at 30 September 1996;

"(c) Urges those Member States that have not yet paid their assessed regular budget contributions, including advances to the Working Capital Fund, for the 1986-1987 to 1996-1997 bienniums, to take the necessary steps to ensure that their contributions are paid promptly and in full;

"(d) Notes with concern the very irregular payment pattern by Member States and the consequences it might have on the Organization's ability to meet its commitments;

"(e) Recommends to the General Conference that the Director-General be authorized to negotiate and

contract, when the Working Capital Fund becomes inadequate to finance budgetary expenditures pending receipt of assessed contributions from Member States, short-term loans from Member States and/or, if necessary, from financial institutions, on the most favourable terms available, to meet the Organization's financial obligations. The total amount of these loans should not exceed, at any one time, the three-month cash requirement of the Organization, or 25 per cent of the approved annual budget, whichever is lower. The amounts borrowed shall be reimbursed as soon as possible from the subsequent receipts of contributions;

"(f) Decides that the interest due on short-term loans shall be charged against miscellaneous income;

"(g) Requests the Director-General to present to subsequent sessions of the policy-making organs a detailed report on any funds borrowed."